FILE COPY

Office - Supreme Court, U. S.
FILED
OCT 16 1946

Nos. 42, 43, 44, 45

In the Supreme Court of the United States

OCTOBER TERM, 1946

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONER

v.

LOUIS A. GREEN AND ROBERT HEILBRUNN, KNOWN IN THESE PROCEEDINGS AS THE GREEN COMMITTEE AND MORRIS GREEN

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONER

v.

CARL B. EARLY, DANIEL MATTHEWS, THOMAS MATTHEWS, ET AL.

VANHORN BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONER

v.

LOUIS A. GREEN AND ROBERT HEILBRUNN, KNOWN IN THESE PROCEEDINGS AS THE GREEN COMMITTEE AND MORRIS GREEN

VANHORN BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONERS

v.

CARL B. EARLY, DANIEL MATTHEWS, THOMAS MATTHEWS, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION

INDEX

	Page
Opinions below	2
Jurisdiction	3
Questions presented	3
Statement	4
Summary of argument	9
Argument	11
I. The court below erred in failing to give the claimants the benefit of the most favorable conflicts rule of any jurisdiction in which action could have been brought apart from bankruptcy	12
II. The court below erred also in its determination of the applicable choice of law rules of the jurisdictions which it regarded as controlling	24
III. While the law of New York is not controlling, the Commission disagrees with the conclusion of the court below as to the substantive law of that state	31
Conclusion	32

CITATIONS

Cases:	
Abbott v. *Stone*, 172 Ill. 634, 50 N. E. 328	26
American Brake Shoe & Foundry Company v. *Interborough Rapid Transit Company*, 26 F. Supp. 954	7, 11, 31
American Surety Co. v *Sampsell*, 327 U. S. 269	18
Amy v. *Dubuque*, 98 U. S. 470	26
Associated Gas and Electric Co., In re (S. D. N. Y., July 17, 1946), C. C. H. Bkcy. L. Rep. par. 55,704	18
Benneson v. *Savage*, 130 Ill. 352, 22 N. E. 838	26
Bowman v. *Neeley*, 137 Ill. 443, 27 N. E. 758	26
Bowman v. *Neely*, 151 Ill. 37, 37 N. E. 840	26
Braniff Investment Co. v. *Norton*, 80 F. 2d 598, certiorari denied, 298 U. S. 663	21
Brierley v. *Commercial Credit Co.*, 43 F. 2d 724, affirmed, 43 F. 2d 730, certiorari denied, 282 U. S. 897	21
Brown v. *Gerdes*, 321 U. S. 178	18
Bryant, Trustee v. *Swofford Bros. Dry Goods Co.*, 214 U. S. 279	17
Central National Bank v. *Bateman & Company, Inc.*, 15 Del. Ch. 31, 131 Atl. 202	26
Champion Shoe Machinery Co., In re, 17 F. Supp. 985	21

Cases—Continued	Page
Chase National Bank v. *Wabash Railway, etc.*, unreported, (E. D. Va., 1941)	31
Chicago, Rock Island and Pac. Ry. Co., In re (*Traphagen* v. *Fleming*), 155 F. 2d 889, petition for certiorari pending, No. 454, this Term	31
Columbia Gas & Electric Corp. v. *United States, et al.*, 151 F. 2d 461, petition for certiorari pending (Nos. 129, 130, 131, this Term)	4, 5
Commonwealth Farm Loan Co. v. *Caudle*, 203 Ky. 761, 263 S. W. 24	25
Continental Illinois Nat. Bank & Trust Co. v. *Chicago, Rock Island & Pac. Ry.*, 294 U. S. 648	17
Cooper's Adm'r v. *Lebus' Adm'rs*, 262 Ky. 245, 90 S. W. 2d 33	12, 27
Cromwell v. *County of Sac*, 96 U. S. 51	21
Drury v. *Wolfe*, 134 Ill. 294, 25 N. E. 626	26
Edwards v. *Bates County*, 163 U. S. 269	26
Erie R. R. Co. v. *Tompkins*, 304 U. S. 64	3, 9, 13, 14, 15
Fry Bros. v. *Theobold*, 205 Ky. 146, 265 S. W. 498	12, 27
Genoa, Town of v. *Woodruff*, 92 U. S. 502	26
Guaranty Trust Company v. *Seaboard Airline Railway*, unreported (E. D. Va., 1943)	31
Guaranty Trust Company v. *York*, 326 U. S. 99	14
Harper v. *Ely*, 70 Ill. 581	26
Heiser v. *Woodruff, et al.*, No. 496, Oct. Term, 1945, decided April 22, 1946	14, 18
Holmberg v. *Armbrecht*, 327 U. S. 392	14
Hornstein v. *Kramer Bros. Freight Lines*, 133 F. 2d 143	29
Joffe v. *Bonn*, 14 F. 2d 50	21
Klaxon Co. v. *Stentor Electric Mfg. Company*, 313 U. S. 487	3, 9, 13, 14
Liverpool Steam Co. v. *Phenix Insurance Co.*, 129 U. S. 397	12, 21, 25
McKenzie, Trustee v. *Irving Trust Company*, 323 U. S. 365	18
McWilliams v. *Northwestern Mutual Life Insurance Company*, 285 Ky. 192, 147 S. W. 2d 79	26
Merchants' & Manufacturers' Securities Co. v. *Johnson*, 69 F. 2d 948, certiorari denied, 293 U. S. 569	21
Meredith v. *Winter Haven*, 320 U. S. 228	29
Mississippi Valley Trust Company v. *Oklahoma Ry. Co.*, 156 F. 2d 283	31
Moody v. *Barker*, 188 Ky. 401, 222 S. W. 89	12, 27
1934 Realty Corp., In re, 150 F. 2d 477, certiorari denied *sub. nom. Prudence Realization Corp.* v. *Hurd Committee*, 326 U. S. 734	18
Pensacola & A. R. R. Co. v. *Hilton's Trustee*, 147 Ky. 553, 144 S. W. 1077	25
Petersen v. *Chicago Great Western Railway Co.*, 138 F. 2d 304	30

Cases—Continued	Page
Prudence Realization Corp. v. *Ferris*, 323 U. S. 650	18
Prudence Realization Corp. v. *Geist*, 316 U. S. 89	18
Realty Associates Securities Corp., In re, 66 F. Supp. 416	31, 32
Scudder v. *Union National Bank*, 91 U. S. 406	12, 21, 25
Seeman v. *Philadelphia Warehouse Co.*, 274 U. S. 403	21
Smith v. *Western & Southern Life Ins. Co.*, 87 F. 2d 839	21
Stekler v. *Pennroad Corp.*, 136 F. 2d 197	30
Swift v. *Tyson*, 16 Pet. 1	10, 19
Talbot Canning Corp., In re, 35 F. Supp. 680	17
United States v. *Pelzer*, 312 U. S. 399	18
Waggaman v. *General Finance Co.*, 116 F. 2d 254	30
Wedding v. *First National Bank*, 280 Ky. 610, 133 S. W. 2d 931	25
West v. *American T. & T. Company*, 311 U. S. 223	29
Wichita Royalty Company v. *City National Bank of Wichita Falls*, 306 U. S. 103	28
William Glenny Glass Co. v. *Taylor*, 99 Ky. 24, 34 S. W. 711	25
Williams v. *Green Bay & Western R. R. Co.*, 326 U. S. 549	14
Wisconsin Central Ry. Co., In re, 64 F. Supp. 251	30
Wisconsin Central Ry. Co., In re, 63 F. Supp. 151	31
Zephyr American Corp. v. *Bates Mfg. Co.*, 128 F. 2d 380	30
Statutes:	
U. S. Constitution, Art. III, Sec. 2	14
Bankruptcy Act:	
Section 63a (1), 11 U. S. C. § 103a (1)	17
Section 118, 11 U. S. C. § 518	16
Section 128, 11 U. S. C. § 528	16
Section 129, 11 U. S. C. § 529	16
Section 208, 11 U. S. C. § 608	2
Federal Judiciary Act of 1789, § 34, 28 U. S. C. § 725	14
Del. Rev. Code (1935) § 3101	26
Trust Indenture Act of 1939, 15 U. S. C. §§ 77aaa, *et seq.*	7
Ill. Rev. Stat. (1935), c. 74, par. 5	26
McKinney's Cons. Laws of N. Y. (Gen. Bus. Law) § 374, Vol. 19	26
Miscellaneous:	
Allen, *What Law Governs the Validity of a Contract in Kentucky* (1939), 28 Ky. L. J. 70	28
Beale, Vol. 2, *Conflict of Laws* (1935), p. 1241	22
Beale, Vol. 3, *Conflict of Laws* (1935), p. 1683	30
Cardozo, *The Nature of the Judicial Process* (1921), pp. 64, *et seq.*	27
Cavers, *A Critique of the Choice-of-Law Problem* (1933), 47 Harv. L. Rev. 173	22
Clark, *State Law in the Federal Courts: The Brooding Omnipresence of Erie* v. *Tompkins* (1946), 55 Yale L. J. 267	30

Miscellaneous—Continued	Page
Collier, Vol. 3, *Bankruptcy* (1941), pp. 1768, 1795, 1796	17
Cook, *"Contracts" and the Conflict of Laws: "Intention" of the Parties* (1938), 32 Ill. L. Rev. 899	25
Goodrich, *Conflict of Laws* (1927), p. 238	22
Jackson, *Full Faith and Credit—The Lawyer's Clause of the Constitution* (1945), 45 Col. L. Rev. 1, n. 1	27
Notes, L. R. A., 1916D 750	22
125 A. L. R. 482	22
Remington, Vol. 2, *Bankruptcy*, (1940) § 955	17
Williston, Vol. 6, *Contracts* (Rev. ed., 1938), §1792, p. 5097	22

In the Supreme Court of the United States

OCTOBER TERM, 1946

No. 42

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONER

v.

LOUIS A. GREEN AND ROBERT HEILBRUNN, KNOWN IN THESE PROCEEDINGS AS THE GREEN COMMITTEE AND MORRIS GREEN

No. 43

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONER

v.

CARL B. EARLY, DANIEL MATTHEWS, THOMAS MATTHEWS, ET AL.

No. 44

VANHORN BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONER

v.

LOUIS A. GREEN AND ROBERT HEILBRUNN, KNOWN IN THESE PROCEEDINGS AS THE GREEN COMMITTEE AND MORRIS GREEN

No. 45

VANHORN BONDHOLDERS PROTECTIVE COMMITTEE, PETITIONER

v.

CARL B. EARLY, DANIEL MATTHEWS, THOMAS MATTHEWS, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION

The Securities and Exchange Commission ("the Commission") became a party to the Chapter X reorganization proceedings pursuant to Section 208 of the Bankruptcy Act, 11 U. S. C. § 608, participated as an appellee before the Circuit Court of Appeals, and is a statutory respondent herein. It submits this brief in support of reversal of the portion of the judgment below presently under review.

OPINIONS BELOW

The District Court rendered no written opinion, but stated the grounds for its decision during the argument (R. 56–57). Thereafter, it entered an order and judgment embodying findings of fact and conclusions of law (R. 192). The opinion of the Circuit Court of Appeals (R. 214) is reported in 151 F. 2d 470.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on October 9, 1945 (R. 213). Rehearing was denied on November 26, 1945 (R. 241). The petition for writs of certiorari of the Vanston Bondholders Protective Committee (Oct. Term, 1945, Nos. 848 and 849) was filed on February 14, 1946, and the petition for certiorari of the Van Horn Bondholders Protective Committee (Oct. Term, 1945, Nos. 850 and 851), on February 15, 1946. Writs of certiorari were granted on March 25, 1946. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, 28 U. S. C. § 347 (a), and Section 24 (c) of the Bankruptcy Act, as amended, 11 U. S. C. § 47 (c).

QUESTIONS PRESENTED

The principal question is whether a bankruptcy court presented with a choice of law problem in determining the validity of a claim against the debtor's estate should apply (1) the conflicts rule of the forum state under *Erie R. R. Co.* v. *Tompkins*, 304 U. S. 64, and *Klaxon Co.* v. *Stentor Electric Mfg. Company*, 313 U. S. 487, (2) an independent federal rule of conflicts, or (3) considering the various conflicts rules of the states in which the debtor would be amenable to suit apart from bankruptcy, that rule most favorable to upholding the claim.

Subsidiary questions include whether the court below correctly interpreted the Kentucky choice of law rule and the substantive law of New York, in so far as either may be found to be determinative.

STATEMENT

The debtor Inland Gas Corporation ("Inland") is a Delaware corporation (R. 101; 197) having its principal assets and principal place of business in Kentucky (R. 104–105; 121; 153). It is a subsidiary of the debtor American Fuel and Power Company ("American Fuel"), a parent holding company, as is also the debtor Kentucky Fuel Gas Corporation ("Kentucky Fuel"). Together with certain other subsidiaries, they comprise the so-called American Fuel and Power System (R. 121–123). Inland and Kentucky Fuel have been under the jurisdiction of federal district courts since 1930, and the others since some years thereafter (R. 113).

On December 2, 1930, an equity receiver was appointed for Inland by the District Court for the Eastern District of Kentucky upon a general creditors' bill to which Inland consented (R. 101; 113). As the court below found in a companion case, *Columbia Gas & Electric Corp.* v. *United States, et al.*, 151 F. 2d 461 (1945), petition for certiorari filed May 29, 1946 (Nos. 129, 130, 131, this Term), the receivership was instigated by Columbia Gas and Electric Corporation

("Columbia") as part of a scheme to stifle the threatened competition of the American Fuel and Power System. Inland defaulted on the semi-annual interest coupons due February 1, 1931, on its first mortgage bonds (R. 187). On April 3, 1931, the indenture trustee declared the entire principal due and payable pursuant to the acceleration provisions of the indenture. This was followed by a bill of foreclosure filed by the indenture trustee on April 14, 1931, which extended the equity receivership and sequestered the income of Inland for the benefit of its first mortgage bondholders. On October 15, 1935, a creditors' petition for the reorganization of Inland under Section 77B of the Bankruptcy Act was filed in the same district court and was approved by an order of the court dated November 23, 1935 (R. 152; 162). The provisions of Chapter X of the Bankruptcy Act were subsequently made applicable to these proceedings (R. 191).

Reorganization has been delayed in part by controversy as to whether the claims of Columbia against Inland and the other debtors should be subordinated to the interests of public security holders,[1] and also by the present dispute as to

[1] Subordination is required under the ruling of the court below which found that Columbia's claims were acquired in violation of the federal anti-trust laws for the purpose of stifling the threatened competition of Inland as part of the American Fuel and Power System. *Columbia Gas & Electric Corp, v. United States, et al.*, 151 F. 2d 461 (1945), petition for certiorari pending (Nos. 129, 130, 131, this Term.)

716564—46——2

whether the claim of the first mortgage bondholders properly includes an item for interest on overdue interest. Delay in the consummation of a plan has enabled the first mortgage bondholders to claim interest on interest in substantial amounts.[2]

The claim here involved is based upon an express covenant in an indenture pursuant to which Inland publicly financed a ten year first mortgage bond issue in 1928 (R. 121–122, 204–205). The indenture was executed in New York, named a New York corporation as trustee, and both bonds and attached interest coupons were made payable in New York, or at the option of the holder, in Chicago, Illinois, where the debtor maintained a paying agent (R. 197–202). The issue was underwritten and sold to the public in the various states by a group of investment bankers (R. 121–122). The covenant in question appears in those provisions of the indenture which relate to the application of monies received by the trustee upon operation or sale of the mortgaged assets after declaration of default (Art. VII Sec. 9; R. 204–205), and, considering the scope and character of the debtor's business, is one which would normally be enforced in a federal liquidation or reor-

[2] Assuming that the ruling of the court below stands with respect to the subordination of the Columbia claims, it appears probable that the mortgaged assets have sufficient value to cover in full the first mortgage bondholders' claim for principal and interest, plus interest on interest.

ganization proceeding.[3] The covenant, moreover, appears to be a rather common one in indentures executed with New York corporate trustees, as is indicated by a survey of indentures on file with this Commission.[4]

The issue of the validity of the covenant was presented to the District Court upon an application for distribution of funds filed by the Van Horn Committee, representing first mortgage bondholders, and the response and petition for advice filed by the reorganization trustee (R. 15–19; 166; 171). The District Court assumed the matter to be governed by the law of New York, where the indenture was executed; and relying on the express holding of Judge Patterson in *American Brake Shoe & Foundry Company* v. *Interborough Rapid Transit Company*, 26 F. Supp. 954 (S. D. N. Y. 1939), that such a covenant was valid in that state, reached a similar conclusion (R. 195). On appeal to the Circuit Court of Appeals for the Sixth Circuit, respondents challenged the District Court's determination on the ground that the New York law prohibited the "compounding of interest," which they asserted would be the effect

[3] See n. 29, *infra*.

[4] Of 57 indentures selected at random from the Commission's files of indentures qualified under the Trust Indenture Act of 1939, 15 U. S. C. §§ 77aaa, *et seq.*, each pertaining to an issue of securities in an amount over $1,000,000, 49 contained covenants for interest on overdue installments of interest. Of these, 18 more recent indentures limited the effectiveness of the covenant to the extent permitted by law.

of allowing the instant claim. They recognized an exception in the local law permitting the collection of simple interest on overdue interest coupons, but contended that it was applicable to detached and negotiated coupons only.

In the absence of any governing state court holding and in light of Judge Patterson's ruling on the precise point, the Commission expressed its agreement with petitioners' view of New York law as upholding the covenant, but also contended that the law of that state was not controlling. The Commission urged that the question be determined in accordance with the general principle of federal bankruptcy law that a claim is to be recognized as valid by a Chapter X court if it is valid and enforceable apart from bankruptcy. The debtor here was amenable to suit in, at least, Delaware (where it was incorporated) and Kentucky (its principal place of business); and the Commission argued that had suit been brought in either of these states, the validity of the covenant would have been upheld.

The Circuit Court of Appeals held, however, that the validity of the covenant for interest was governed by the *lex loci contractus*, assumed to be that of New York (R. 219). Examining the "confused status" of the substantive law of New York, the court concluded that the claim should be disallowed (R. 226).

SUMMARY OF ARGUMENT

While the basis of its ruling is not entirely clear, the court below apparently determined that the jurisdictional source of the applicable choice of law rule respecting the validity of the covenant was either the law of Kentucky, as the forum state, or the federal law. In our view it was error to have referred to the forum state, as such, since the doctrine of *Erie R. R. Co.* v. *Tompkins*, 304 U. S. 64, and *Klaxon Co.* v. *Stentor Electric Mfg. Company*, 313 U. S. 487, is inapplicable in a proceeding arising under the federal bankruptcy jurisdiction. It was also erroneous to determine, as a matter of federal conflicts law, that the law of New York, as the place of formal execution of the indenture, governed the validity of the covenant.

Since, apart from certain equitable considerations not involved here, a claim is entitled to be recognized as valid in bankruptcy if it is valid and enforceable apart from bankruptcy, the court should have given the claimants the benefit of the most favorable conflicts rule of any of the forums in which suit could have been brought if the debtor were not in bankruptcy. In the present case, suit could have been instituted either in Delaware, the debtor's state of incorporation, or in Kentucky, its principal place of business and the location of the mortgaged assets. While the court below inquired into the applicable Kentucky law, we believe it erred in concluding that the covenant would not have been enforced

by the Kentucky state courts. It relied upon generalized pronouncements of Kentucky courts in cases involving dissimilar considerations. Furthermore, the court below failed to inquire into the Delaware law which would have been applied in a suit upon the covenant. In our view Delaware law, like that of Kentucky, would have sustained the covenant. We think that both Kentucky and Delaware would have held that, in the absence of an overriding policy of any state possessing a greater interest in the matter, the proper rule of conflicts is to give effect to the presumed intention of the parties that the covenant be valid and enforceable, and accordingly to apply the substantive law of any state having a substantial relationship to the transaction under which the covenant would be regarded as valid. In this connection it is relevant that the federal decisions in diversity cases during the *Swift* v. *Tyson* era seemed to apply a similar conflicts rule.

Since the covenant here was admittedly valid as a matter of substantive law in Kentucky, the location of the mortgaged assets and the debtor's principal place of business, in Illinois, the alternative place of performance, and in Delaware, the debtor's place of incorporation, and since the assumed contrary policy of New York could relate only to the protection of local residents against improvident contracts and not to transactions between a non-resident corporate borrower and a group of nationwide public investors, the covenant

would be valid under the substantive law of every state having a substantial relationship to the transaction. Accordingly, it should be recognized as valid for purposes of bankruptcy.

While the Commission does not regard the substantive law of New York as controlling, it believes that the court below also erred in its determination that the covenant was invalid under that law. In the Commission's view an express covenant to pay interest on overdue interest coupons is valid in New York for the reasons set forth in Judge Patterson's opinion in *American Brake Shoe & Foundry Company* v. *Interborough Rapid Transit Company*, 26 F. Supp. 954 (S. D. N. Y., 1939). Detailed argument on this point, however, has been left to the interested private parties.

ARGUMENT

The court below ruled that a federal bankruptcy court sitting in Kentucky must hold invalid an indenture covenant for interest on overdue installments of interest in a multi-state public financing because, in the opinion of the court below, such a covenant would not be enforced in New York, where the indenture was executed. In reaching its ultimate conclusion, the court had to determine, first, the jurisdiction from which to seek a choice of law rule; second, the applicable choice of law rule of that jurisdiction; and third, the substantive law of the jurisdiction to which reference was eventually to be made. The petitioners and the Commission challenge the correctness of each determination of the Circuit Court of

Appeals, and the anomalous result reached by the combination of such determinations whereby a covenant in common use, generally accepted by the financial community and admittedly valid in the jurisdictions possessing the most substantial interests in the financing involved, is invalidated because of an assumed local policy of a state having a comparatively minor interest in the matter, despite (1) the absence of any clear-cut indication of invalidity in the decisional or statutory law of that state, and (2) the express holding of a federal district court sitting in that state, and presumably as familiar with local law as any federal court is likely to be, that the covenant is valid under the law of the state.

I. THE COURT BELOW ERRED IN FAILING TO GIVE THE CLAIMANTS THE BENEFIT OF THE MOST FAVORABLE CONFLICTS RULE OF ANY JURISDICTION IN WHICH ACTION COULD HAVE BEEN BROUGHT APART FROM BANKRUPTCY.

In determining that the substantive law of the place of contracting, assumed to be New York, governed the validity of the claim involved in these proceedings, the court below relied upon two non-bankruptcy federal cases[5] and three Kentucky cases,[6] all dealing in general terms with problems

[5] *Scudder* v. *Union National Bank*, 91 U. S. 406, and *Liverpool Steam Co.* v. *Phenix Insurance Co.*, 129 U. S. 397. We note later our disagreement with the interpretation of these precedents by the court below. See pp. 20–21, *infra*.

[6] *Moody* v. *Barker*, 188 Ky. 401, 222 S. W. 89 (1920); *Fry Bros.* v. *Theobold*, 205 Ky. 146, 265 S. W. 498 (1924); and *Cooper's Adm'r* v. *Lebus' Adm'rs*, 262 Ky. 245, 90 S. W. 2d 33 (1936).

of the conflict of laws as applied to contracts (R. 219, 221). While the court below did not explicitly commit itself to a choice between federal and Kentucky law as the jurisdictional source of the choice of law rule—its theory apparently being that the same result would obtain under either law—it referred to the Kentucky decisions only because the bankruptcy court was located in that state and the conflicts rule of the forum state might be binding upon a bankruptcy court under the doctrine of *Erie R. R. Co.* v. *Tompkins*, 304 U. S. 64, as applied to conflicts questions by *Klaxon Co.* v. *Stentor Electric Mfg. Co.*, 313 U. S. 487. Petitioners have construed the ruling below as requiring a bankruptcy court to follow the conflicts rule of the forum state in all matters (Petition, Oct. Term, 1945, Nos. 848, 849, p. 7; Petition, Oct. Term, 1945, Nos. 850, 851, p. 3). On the other hand, some of the respondents have taken the view that the court below applied what is, in essence, an independent federal choice of law rule (Early Brief in Opposition to Petition, p. 9). We believe that on either interpretation the determination below was erroneous.

If petitioners are correct in interpreting the ruling below to mean that a bankruptcy court, in

716564—46——3

determining the validity of a claim against a debtor's estate arising out of a multi-state transaction, is bound to follow the choice of law rule of the forum state under the *Erie* and *Klaxon* decisions, we believe that such a ruling would be an extension of the doctrine of these cases to an area in which it has no relevant application. The decisions of this Court during the past two terms have made it clear that the *Erie* doctrine is applicable only to an action brought in a federal court merely because it is "between Citizens of different States" under Article III, Section 2 of the Constitution. *Guaranty Trust Company* v. *York*, 326 U. S. 99; *Williams* v. *Green Bay & Western R. R. Co.*, 326 U. S. 549; *Holmberg* v. *Armbrecht*, 327 U. S. 392; *Heiser* v. *Woodruff*, No. 496, Oct. Term, 1945, decided April 22, 1946. As the Court stated in the *Holmberg case* (327 U. S. at 394), "For purposes of diversity suits a federal court is, in effect, 'only another court of the State'." The opinion in the *Erie* case observed that "diversity of citizenship jurisdiction was conferred in order to prevent apprehended discrimination in state courts against those not citizens of the State." 304 U. S. 64, 74. Accordingly, Section 34 of the Federal Judiciary Act of 1789, 28 U. S. C. § 725, was not to be construed so as to create an independent body of federal "general law" applicable to rights having their origin in state law, merely because a non-

resident plaintiff availed himself of the privilege of suing in a federal court.

The bankruptcy jurisdiction of a federal court, however, is quite different. As we endeavor to show below, the nature and purpose of the federal bankruptcy jurisdiction are such as to render inapplicable the considerations underlying the *Erie* doctrine. The rationale of that doctrine is that in a diversity proceeding there should be no difference in result whether the non-resident plaintiff institutes his action in a state court or elects to bring suit in a federal court sitting in that state. Claimants against a bankrupt estate, however, have no choice between state or federal forums but are compelled to present their claims in a single bankruptcy court. Had there been no bankruptcy, these claims might well have been enforced in states other than that in which the bankruptcy court sits. Whatever the relevance in bankruptcy of considerations pointing to the desirability of uniform results as between federal and state tribunals, those considerations cannot require the bankruptcy court to conform to the law of the state in which it sits, if, apart from bankruptcy, suit might well have been brought in a court of some other state which would apply a different rule of law.

Moreover, in looking to the conflicts rule of the

forum state, the court below was attaching a significance to the forum which is hardly warranted by the place it holds in the federal bankruptcy scheme. Venue in bankruptcy proceedings is determined principally by the convenience of the parties, and not by any considerations relating to the substantive character of the claims involved. Ordinarily, the Chapter X forum is where the debtor's principal place of business or principal assets are located. Sec. 128, 11 U. S. C. § 528. But where the debtor is a subsidiary corporation, a petition may also be filed in the court which has approved a petition by or against the parent. Sec. 129, 11 U. S. C. § 529. And, in any event, regardless of the location of the principal assets of the debtor or its principal place of business, the judge may transfer a Chapter X proceeding to a court of bankruptcy in any other district, if the interests of the parties will be best served by such transfer. Sec. 118, 11 U. S. C. § 518.

Clearly, therefore, the court below erred in so far as it may have held that a federal bankruptcy court, in determining the validity of claims asserted, is bound to follow the conflicts rule of the state in which it sits. It does not follow, however, that a bankruptcy court should adopt an independent federal choice of law rule, such as, for example, to refer directly to the substantive law of the place of contracting or of the place of performance or

of some other state having a substantial relationship to the transaction. Congress might have done so by express legislation, as indeed it might have expressly enacted provisions of substantive law governing the recognition of claims for interest against a bankrupt estate.[7]

But Congress has not seen fit to legislate with respect to these matters. From the general pattern of the statute, however, the federal courts have derived the general principle that a claim is valid in bankruptcy if it is valid and enforceable apart from bankruptcy,[8] provided, of course, that there are no equitable considerations calling for different treatment because of the fed-

---

[7] As to the potential scope of permissible legislation under the federal bankruptcy power, see *Continental Illinois Nat. Bank & Trust Co.* v. *Chicago, Rock Island & Pac. Ry.*, 294 U. S. 648. Congress has already touched upon the subject of the status of claims for interest in excluding from provable claims filed by unsecured creditors against an insolvent estate items of interest accruing after the date of a petition in bankruptcy. Section 63a (1), 11 U. S. C. § 103a (1). That section, however, is only procedural in character since it does not preclude the payment of interest on a claim should it later develop that there are sufficient assets remaining after the satisfaction of the principal indebtedness; and, to the extent that a creditor has security sufficient to pay interest on his claim after satisfaction of the principal debt, the section is also inapplicable. See 3 *Collier on Bankruptcy* (14th ed., 1941) § 63.16, and cases cited.

[8] See *Bryant, Trustee* v. *Swofford Bros. Dry Goods Co.*, 214 U. S. 279; *In re Talbot Canning Corp.*, 35 F. Supp. 680 (D. Md., 1940); 3 Collier, *Bankruptcy* (1941) pp. 1768, 1795, 1796; 2 Remington, *Bankruptcy* (1940) § 955.

eral policy of distribution in bankruptcy.[9] However, the principle upon which the substantive law of a particular state is applied in the determination of a validity of a claim is derived not from considerations underlying the doctrine of the *Erie* case, but from the federal statute itself which is construed to require reference to state law in such matters. In *American Surety Co. v. Sampsell*, 327 U. S. 269, 272, this Court said: "True, we stated in both *Prudence* opinions that the federal law governing distribution of a bankrupt's estate should be applied with 'appropriate regard for rights acquired under rules of state law . . .' But the extent to

[9] As this Court recently observed in *Heiser* v. *Woodruff, et al.*, No. 496, Oct. Term, 1945, decided April 22, 1946, a bankruptcy court is not required "to adopt local rules of law in determining what claims are provable, or to be allowed, or how the bankrupt's estate is to be distributed among claimants." In determining what claims are provable and "what objections may be made to their proof, and in determining the extent to which the inequitable conduct of a claimant in acquiring or asserting his claim in bankruptcy, requires its rejection or its subordination to other claims which, in other respect are of the same class, the bankruptcy court is defining and applying federal, not state, law." Compare *Prudence Realization Corp.* v. *Geist*, 316 U. S. 89, 95–96; *United States* v. *Pelzer*, 312 U. S. 399, 402–3; *Prudence Realization Corp.* v. *Ferris*, 323 U. S. 650; *American Surety Co.* v. *Sampsell*, 327 U. S. 269; *Brown* v. *Gerdes*, 321 U. S. 178; *McKenzie, Trustee* v. *Irving Trust Company*, 323 U. S. 365; *In re 1934 Realty Corp.*, 150 F. 2d 477 (C. C. A. 2, 1945), certiorari denied *sub. nom. Prudence Realization Corp.* v. *Hurd Committee*, 326 U. S. 734; *In re Associated Gas and Electric Co.* (S. D. N. Y., July 17, 1946) C. C. H. Bkcy. L. Rep. par. 55,704.

which state law is to be considered is in the last analysis a matter of federal law." [10]

As illustrated by the present case, reference to state law for the determination of the validity of a claim in bankruptcy arising from a multi-state transaction often gives rise to choice of law problems. While the Bankruptcy Act makes no provision for the choice of law rules which should govern in proceedings under that statute, there is a substantial body of federal decisions on conflict of laws problems.[11] These cases, for the most part, arose in the *Swift* v. *Tyson* [12] era, so that the decisions therein to apply independent federal rules of conflicts in diversity proceedings are now overruled. However, the principles enunciated in these cases are still relevant in dealing with questions where a federal court is not bound by

[10] The validity, as a matter of public policy, of a covenant for interest on interest, as applied to interest accruing since the date of a federal equity receivership or bankruptcy proceeding, might conceivably be regarded as a proper subject for independent decision by the federal court, even in the absence of direct legislation. The consequence of such a holding would be to afford greater uniformity and certainty in dealing with a problem which appears to be arising with increasing frequency in reorganization proceedings and occasionally in the state courts. See cases cited *infra* n. 29. We recognize, however, that there is no precedent for such a rule. The closest analogy would appear to be those cases holding that the equitable status of certain claims is a matter of bankruptcy law. See n. 9, *supra*.

[11] See p. 21, *infra*.

[12] 16 Pet. 1.

state choice of law rules. Accordingly, if there were no overriding policy of the Bankruptcy Act to recognize claims in bankruptcy as valid if they were valid and enforceable apart from proceedings under the statute, we believe that the bankruptcy court should apply a federal choice of law rule. Even in such event, however, we do not agree with the court below that application of the federal choice of law precedents governing the validity of a covenant for interest on interest would have invalidated the instant claims under the substantive law of the place of contracting, assumed to be New York. We do not regard the federal cases [12] cited by the court below as authority for such a conclusion. On the contrary, the rule set forth in the many federal decisions dealing specifically with interest questions would uphold the covenant if, without regard to the substantive law of the place of contracting, the covenant is valid in a state where the bondholders had an option to receive payment, or where the mortgaged assets are located, or perhaps where the debtor is incorporated or has its principal place of business.

Federal courts have referred to the law of the place of contracting where that state bore a more substantial, if not dominant, relationship to the transaction involved and no other state possessed a contrary overriding policy, the theory being that

[12] See n. 5, *supra*.

the parties intended the law of that state to apply. Such were the cases relied upon by the court below: *Scudder* v. *Union National Bank,* 91 U. S. 406, and *Liverpool Steam Co.* v. *Phenix Insurance Co.,* 129 U. S. 397. As respects agreements for interest, however, the federal policy, so far as it can be derived from usury cases, has, like that of most states, departed from the ancient prejudice against interest claims and has tended to uphold the agreement of the parties in such matters. These cases, generally speaking, have referred to any state bearing a substantial relationship to the transaction under the law of which the contract is valid, provided that there is no clearly contrary overriding policy of another state possessing a more substantial interest in the matter. *Seeman* v. *Philadelphia Warehouse Co.,* 274 U. S. 403; *Cromwell* v. *County of Sac,* 96 U. S. 51; *Smith* v. *Western & Southern Life Ins. Co.,* 87 F. 2d 839 (C. C. A. 5, 1937); *Joffe* v. *Bonp,* 14 F. 2d 50 (C. C. A. 3, 1926); *Brierley* v. *Commercial Credit Co.,* 43 F. 2d 724 (E. D. Pa., 1929), affirmed, 43 F. 2d 730 (C. C. A. 3, 1930), certiorari denied, 282 U. S. 897; *Braniff Investment Co.* v. *Norton,* 80 F. 2d 598 (C. C. A. 5, 1935), certiorari denied, 298 U. S. 663; *Merchants' & Manufacturers' Securities Co.* v. *Johnson,* 69 F. 2d 940 (C. C. A. 8, 1934), certiorari denied, 293 U. S. 569; *In re Champion Shoe Machinery Co.,* 17 F. Supp. 985 (E. D. Mo., 1937); see also state cases

collected in Notes, L. R. A. 1916D 750 and 125 A. L. R. 482.[14]

However, as has been indicated, if application of an independent federal rule of conflicts in the determination of the validity of a claim in bankruptcy in a particular case would run counter to the underlying purpose of the statute to accord the claim the validity it possesses apart from bankruptcy, we believe that such application could not properly be made. A claim, such as the one here involved, which is not predicated upon federal law must necessarily find its origin in state law. Accordingly, unless some state having a relevant connection with the claim would recognize it as valid under its own law, it would be axiomatic that the bankruptcy court could not entertain it. Where state rules with respect to choice of law enter into the determination of the validity of a claim apart from bankruptcy, as they do to the extent that validity may be thought to depend on enforceability in an available forum, the bankruptcy court should look to the results which would have prevailed in such forums as would have been available apart from bankruptcy. In a sense this is a special rule as to choice of law applicable in bankruptcy and based upon impli-

[14] See also 2 Beale, *Conflict of Laws* (1935), p. 1241; Goodrich, *Conflict of Laws* (1927), p. 238; 6 Williston, *Contracts* (Rev. ed., 1938) § 1792, p. 5097; Cavers, *A Critique of the Choice-of-Law Problem* (1933), 47 Harv. L. Rev. 173, at 182.

cations drawn from the bankruptcy law itself that claims provable in bankruptcy should correspond to claims enforceable outside of bankruptcy. To hold otherwise where the local law is clear would involve the anomalous result that a claim which could not have been the basis for successful action outside of bankruptcy is nevertheless provable in bankruptcy, or *vice versa*.[18]

In accordance with this approach, the Commission urges here, as it did in the court below, that the bankruptcy court should have given the first mortgage bondholders the benefit of either the conflicts rule of Kentucky (where Inland has its principal place of business), or that of Delaware (where Inland was incorporated), whichever might appear more favorable in view of the fact that, apart from bankruptcy, suit could have been brought in either state. And if a federal conflicts rule should be deemed applicable, we believe that the same result would be reached, because in our view a bankruptcy

[18] The question of choice of law in determining the validity of a claim might not affect the character of the claim as a liquidated one; yet, one could hardly visualize permitting an involuntary bankruptcy proceeding to be instituted through the use of claims which could not be the basis of recovery outside of bankruptcy. Conversely, where voluntary bankruptcy proceedings are instituted because of a debtor's inability to meet claims enforceable outside of bankruptcy, it would hardly fulfill the purpose of the proceedings to disallow these claims in bankruptcy. Likewise, problems of financial accounting would be vastly complicated if potential liabilities would have to be set up so as to reflect differences of enforceability, depending upon the contingency of whether or not bankruptcy proceedings should develop.

court, correctly following the applicable federal precedents, would have applied a choice of law rule under which the covenant would be upheld.

II. THE COURT BELOW ERRED ALSO IN ITS DETERMINATION OF THE APPLICABLE CHOICE OF LAW RULES OF THE JURISDICTIONS WHICH IT REGARDED AS CONTROLLING

In reaching its determination that both federal and Kentucky law required reference to the substantive law of New York, the court below cited no directly applicable precedents but appears to have relied upon generalized pronouncements of the federal and Kentucky courts in unrelated situations. As a result, it invalidated the agreement of the parties upon the basis of an assumed public policy of a state having, we submit, little if any relevance to the particular transaction.

The artificiality of applying a rule which invalidates the present covenant under an assumed rule of New York law, as the "place of contracting", is emphasized where, as here, the real parties in interest, both now and in contemplation at the time, were the Delaware incorporated debtor and a nation-wide group of investors who presumably purchased their bonds in the several states where they resided. Had a Delaware or Kentucky indenture trustee been selected, the contract between the debtor and indenture trustee would probably have been executed in Delaware or Kentucky and the instant problem would not have

arisen. The mere fact that the indenture was executed in New York with a New York trustee should not give overriding significance to a rule of New York substantive law derived from a public policy which could relate only to protecting local debtors from improvident contracts, not to preventing New York trust companies from functioning as indenture trustees under forms of indentures not contrary to the policy of the issuer's place of incorporation or principal place of business.[18]

We have already expressed our disagreement with the conclusion of the court below as to the federal rule of conflicts to be derived from the *Scudder* and *Liverpool* cases. See pages 19–21, *supra*. As to Kentucky law, the Court of Appeals of that State, while following the law of the place of contracting in other types of cases, appears to have adopted the "presumed intent" rule in usury cases involving the validity of interest provisions. See *William Glenny Glass Co.* v. *Taylor*, 99 Ky. 24, 34 S. W. 711 (1896); *Wedding* v. *First National Bank*, 280 Ky. 610, 133 S. W. 2d 931 (1939); *Commonwealth Farm Loan Co.* v. *Caudle*, 203 Ky. 761, 263 S. W. 24 (1924); *Pensacola & A. R. R. Co.* v. *Hilton's Trustee*, 147 Ky. 553, 144 S. W. 1077 (1912). The court below recognized that the covenant for interest on interest was valid under

[18] Compare Professor Walter Wheeler Cook's analysis of a similar fact situation in *"Contracts" and the Conflict of Laws: "Intention of the Parties* (1938), 32 Ill. L. Rev. 899, 908 *et seq.*

the local substantive law of Kentucky,[17] the location of the mortgaged assets and of Inland's principal place of business, and of Illinois,[18] the alternate place for payment of the bonds and coupons (151 F. 2d at 475; R. 220). It appears also that the covenant is valid in Delaware, where Inland was incorporated.[19] Thus, in addition to Illinois, the alternate place of performance, the covenant is valid as a matter of substantive law in Delaware and Kentucky, and the relationship of these three states to the financing operation here involved is far more substantial, as a practical matter, than that of New York.[20] Moreover, there is no federal public policy against enforcement in a federal court of the covenant to pay simple interest on overdue interest coupons.[21]

---

[17] See *McWilliams* v. *Northwestern Mutual Life Insurance Company*, 285 Ky. 192, 147 S. W. 2d 79 (1940), and cases cited therein.

[18] See *Bowman* v. *Neeley*, 137 Ill. 443, 27 N. E. 758 (1891); *Bowman* v. *Neely*, 151 Ill. 37, 37 N. E. 840 (1894); *Harper* v. *Ely*, 70 Ill. 581 (1873); *Benneson* v. *Savage*, 130 Ill. 352, 22 N. E. 838 (1889); *Drury* v. *Wolfe*, 134 Ill. 294, 25 N. E. 626 (1890); *Abbott* v. *Stone*, 172 Ill. 634, 50 N. E. 328 (1898).

[19] *Central National Bank* v. *Bateman & Companies, Inc.*, 15 Del. Ch. 31, 131 Atl. 202 (1925).

[20] Perhaps relevant to the public policy of the states involved are statutes in Delaware, Illinois and New York which render the defense of usury unavailable to corporate debtors: see Del. Rev. Code (1935), § 3101; Ill. Rev. Stat. (1935), c. 74, par. 5; 19 McKinney's Cons. Laws of N. Y. (Gen. Bus. Law), § 374.

[21] See *Town of Genoa* v. *Woodruff*, 92 U. S. 502; *Amy* v. *Dubuque*, 98 U. S. 470, 473; *Edwards* v. *Bates County*, 163 U. S. 269, 272.

The court below, however, relied upon generalized statements of the Kentucky court in dissimilar cases,[22] to the effect that the validity of a contract is to be determined by the law of the place of contracting, which it assumed to be that of New York, where the indenture was executed. Its ruling is reminiscent of a judicial approach recently criticized by Mr. Justice Jackson—i. e., one which assumes "that the process of judging state law by a federal court can be so mechanical that, without the use of judgment of its own, it can pick out and apply state precedents which determine the law of the state."[23] As Mr. Justice Jackson stated, "the process of finding decisional law [cannot] be so simplified."[24]

We respectfully submit that the court below, in conscientiously attempting to follow such guide

---

[22] *Moody* v. *Barker*, 188 Ky. 401, 222 S. W. 89 (1920) (wife's liability as surety on husband's note); *Fry Bros.* v. *Theobold*, 205 Ky. 146, 265 S. W. 498 (1924) (effect of seller's failure to record conditional sale as against creditor or innocent purchaser from buyer); *Cooper's Adm'r* v. *Lebus' Adm'rs*, 262 Ky. 245, 90 S. W. 2d 33 (1936) ("insurable interest" in life of business partner). In none of these cases did it appear that a state other than the place of contracting possessed any peculiar relationship to the transaction involved.

[23] Jackson, *Full Faith and Credit—The Lawyer's Clause of the Constitution* (1945) 45 Col. L. Rev. 1, n. 1, containing the text of an address at the Fourth Annual Benjamin N. Cardozo lecture delivered December 7, 1944, under the auspices of the Committee on Post-Admission Legal Education of the New York City Bar Association.

[24] *Ibid.* See also Cardozo, *The Nature of the Judicial Process* (1921), pp. 64, *et seq.*

posts to Kentucky law as were furnished by the decisions of its state courts, took too literally the broad generalizations appearing in such decisions. It may not have sufficiently appreciated that "principles" announced in conflicts cases are often deceptive because of their easy generality, and that choice of law problems bring forth different criteria and varying solutions depending upon particular circumstances. Perhaps in no other field of law is there as much ambiguity of terminology and divergence of criteria. A commentator on the Kentucky law of conflicts relating to contracts has pointed out that, at one time or another, the Kentucky court itself has expressed all of the divergent views—i. e., the law of the place of contracting, the law of the place of performance, and the intention of the parties—and that no single dominant rule can be derived from the Kentucky decisions.[25] Such a situation, probably similar to that in many other states, illustrates the difficulties under which a federal court in such a situation labors; and emphasizes the importance of examining conflicts decisions for their actual holdings and underlying rationale. Were the present case before the highest court of Kentucky, that court would resolve the instant controversy in light of its best judgment as to what would be a proper rule of conflicts in the premises, with due regard to any existing precedents in similar cases. A federal court interpreting state law is charged with the same duty. See *Wichita Royalty*

[25] See Allen, *What Law Governs the Validity of a Contract in Kentucky*, (1939) 28 Ky. L. J. 70.

Company v. *City National Bank of Wichita Falls*, 306 U. S. 103; *West* v. *American T. & T. Company*, 311 U. S. 223, 237; *Meredith* v. *Winter Haven*, 320 U. S. 228, 234, 237–8. In view of the comparatively minor interest of New York in the transactions involved, the importance to public investors and to the financial community of upholding the obligations of corporate securities so widely sold, the absence of any clear indication of invalidity under the New York law, and the general validity of the covenant elsewhere, we believe that the Kentucky state courts would have reached a conclusion different from that of the court below.

As previously noted, the court below made no inquiry into the Delaware law of conflicts. We are aware of no Delaware case in point, but in the absence of a controlling local precedent to the contrary, it would be reasonable for a federal court to conclude that the Delaware court would adhere to the rule generally prevailing elsewhere with respect to contracts for interest.[26] The result would be to uphold the contract.[27]

[26] *Cf. Zephyr American Corp.* v. *Bates Mfg. Co.*, 128 F. 2d 380, 387 (C. C. A. 3, 1942); *Hornstein* v. *Kramer Bros. Freight Lines*, 133 F. 2d 143 (C. C. A. 3, 1943).

[27] In the event that this Court should hold either (1) that a proper interpretation of the choice of law rule of Kentucky would uphold the contract as valid under the substantive laws of Kentucky, Delaware or Illinois, or (2) that the court below erred in assuming such an agreement to be contrary to the public policy of New York, it would not be necessary to consider the Delaware choice of law rule. If, however, decision of the case should necessitate inquiry into the Delaware choice of law rule, we believe that, in the interest

On the assumption that an independent federal rule of conflicts may not be applied for the purpose of determining the validity of claims against the estate, it would seem that the field of the conflict of laws—being inherently interstate in character and involving often problems of comity among states and issues of constitutional significance—is one in which the federal courts might properly exercise a certain degree of initiative for the purpose of developing in the various local jurisdictions uniform standards suitable to the needs of a united nation. Where the local law, because of its silence on the particular problem or otherwise, provides no guiding standards, it has been suggested that a federal court should refrain from purely mechanical adjudication and should assume that the local courts will ultimately follow that choice of law rule which commends itself to the federal court as most consonant with interstate comity.[28]

---

of terminating the litigation, this Court itself should decide that question rather than remand for determination by the lower court. Including the period of the equity receivership, the debtor has been in reorganization nearly 16 years.

[28] Clark, *State Law in the Federal Courts: The Brooding Omnipresence of Erie* v. *Tompkins*, (1946) 55 Yale L. J. 267, at 295–296; cf. *Stekler* v. *Pennroad Corp.*, 136 F. 2d 197, 199 (C. C. A. 3, 1943).

Compare the presumption which exists in many states that the conflicts rule of a particular state is the same as that of the forum, unless the contrary is shown. See, e. g., *In re Wisconsin Central Ry. Co.*, 64 F. Supp. 251, 256 (D. Minn., 1946); *Petersen* v. *Chicago, Great Western Railway Co.*, 138 F. 2d 304 (C. C. A. 8, 1943); *Waggaman* v. *General Finance Co.*, 116 F. 2d 254 (C. C. A. 3, 1940). See also 3 Beale, *Conflict of Laws* (1935), p. 1683.

III. WHILE THE LAW OF NEW YORK IS NOT CONTROLLING, THE COMMISSION DISAGREES WITH THE CONCLUSION OF THE COURT BELOW AS TO THE SUBSTANTIVE LAW OF THAT STATE

It does not appear that the New York Court of Appeals has yet ruled upon the validity of an express covenant to pay simple interest on overdue coupons attached to a corporate bond, and certainly not in the setting of a multi-state financing. This may be due to the fact that the problem is not likely to arise in the state courts, for following default a corporation generally finds itself in liquidation or reorganization under the Bankruptcy Act.[29] The precise question, however, was presented to a federal court in New York in *American Brake Shoe & Foundry Company* v. *Interborough Rapid Transit Company*, 26 F. Supp. 954 (1939) where then District Judge Patterson, sitting in the Southern District of New York, reviewed the New York decisions and found

[29] For example, the question was involved in the recent reorganization cases of *In re Chicago, Rock Island and Pac. Ry. Co.* (*Traphagen* v. *Fleming*), 155 F. 2d 889 (C. C. A. 7, 1946), petition for certiorari pending, No. 454, this Term, *In re Realty Associates Securities Corp.*, 66 F. Supp. 416 (E. D. N. Y., 1946), *Guaranty Trust Company* v. *Seaboard Airline Railway*, unreported (E. D. Va., 1943), and *Chase National Bank* v. *Wabash Railway, etc.*, unreported (E. D. Va., 1941), all upholding claims for interest on interest, the latter three cases being decided under the substantive law of New York, and *Mississippi Valley Trust Company* v. *Oklahoma Ry. Co.*, 156 F. 2d 283 (C. C. A. 10, 1946) and *In re Wisconsin Central Ry. Co.*, 63 F. Supp. 151 (D. Minn. 1945) (appeal pending), disallowing claims for interest on interest, the latter also under the law of New York.

nothing therein which would invalidate an express covenant for simple interest on overdue installments of interest. Accordingly, he concluded that the covenant was valid and enforceable. While the Commission regards the opinion of Judge Patterson as reflecting an accurate and informed view of the New York law,[30] we have left detailed argument on this point to the interested private parties.

CONCLUSION

The judgment of the court below to disallow petitioners' claims for interest on the overdue interest coupons in accordance with the indenture covenant should be reversed.

Respectfully submitted.

J. HOWARD MCGRATH,
Solicitor General.

PHILIP ELMAN,
Special Assistant to the Attorney General.

ROGER S. FOSTER,
Solicitor,

CHARLES J. ODENWELLER, JR.,
Cleveland Regional Administrator,

ALEXANDER COHEN,
Attorney,
Securities and Exchange Commission.

OCTOBER 1946.

[30] His conclusion was recently adhered to by District Judge Moscowitz, sitting in the Eastern District of New York, in *In re Realty Associates Securities Corp.*, 66 F. Supp. 416 (1946), which, although not involving interest coupons, did allow simple interest on overdue interest, contrary to the assumption of the court below as to the law of that state.

U. S. GOVERNMENT PRINTING OFFICE: 1946